

Unsecured Credit Hearing



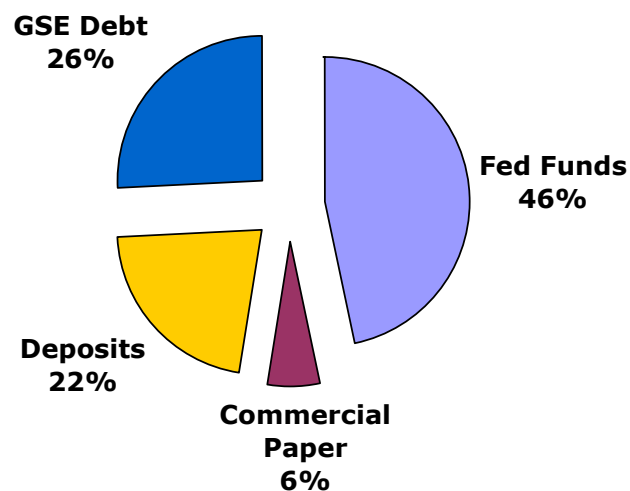
**Office of Supervision
March 12, 2003**

Unsecured Credit

As of January 31, 2003, the Federal Home Loan Banks (FHLBanks) had total unsecured credit outstanding of \$87.0 billion. These unsecured investments consist principally of:

- ❑ Overnight and term federal funds sold to investment-grade-rated banks (46%)
- ❑ Deposits in investment-grade-rated banks (22%)
- ❑ Commercial paper issued by investment-grade-rated issuers (6%)
- ❑ Debt obligations of other government-sponsored enterprises (GSEs) (26%).

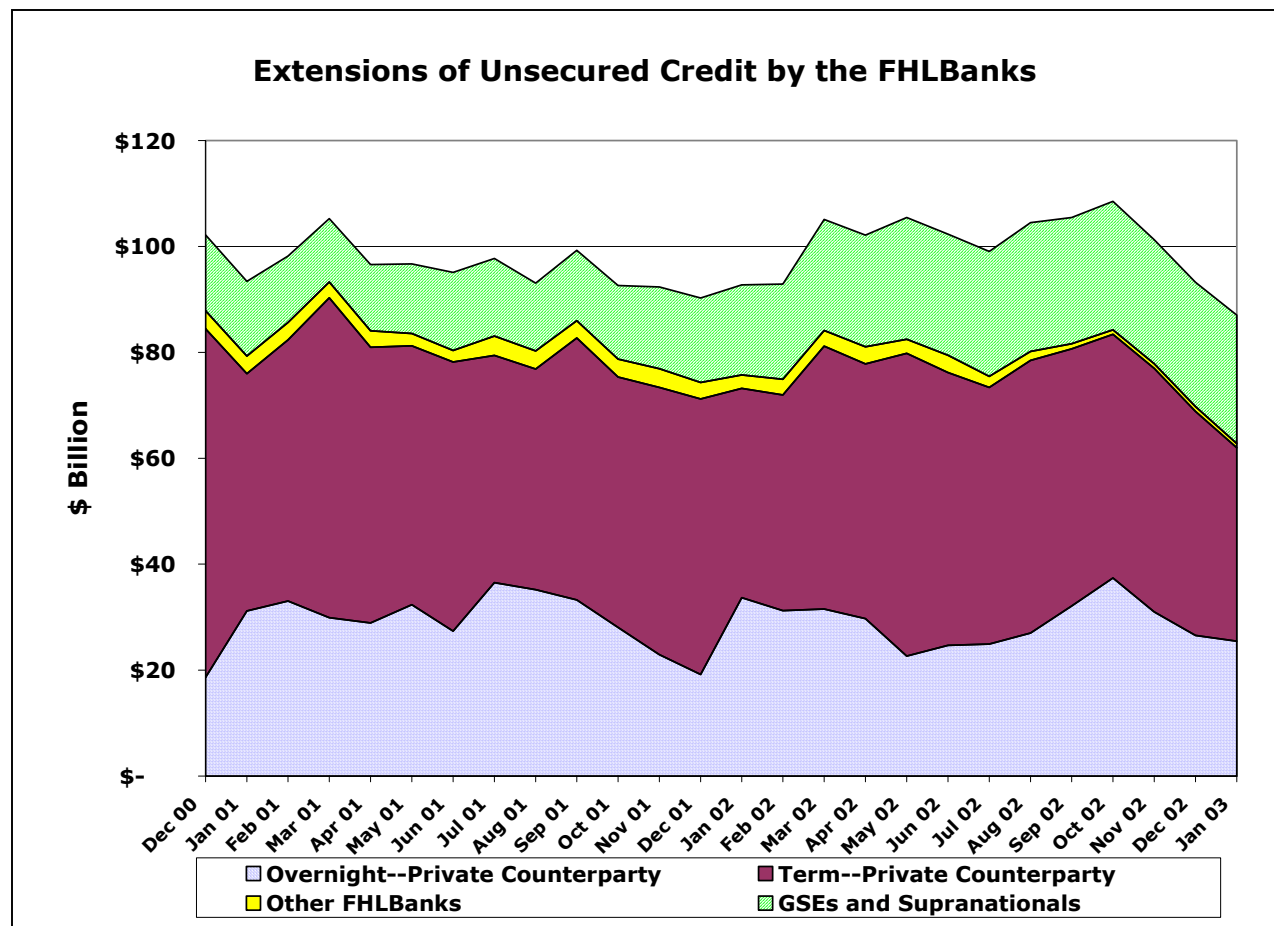
**Extensions of Unsecured Credit by the FHLBanks
At January 31, 2003**



Since the end of 2000, unsecured investments have averaged (in billions) as follows:

Total Extensions of Credit	98.2
less Investments in FHLBank Debt	2.6
equals External Extensions	96.2
less GSEs and Supranationals	18.1
equals Private Extensions	77.6
Term	48.5
Overnight	29.0

The principal trends have been an increase in the holdings of the debt of other GSEs over the past two years and a decrease in both overnight and term extensions of credit to private counterparties over the past four months.

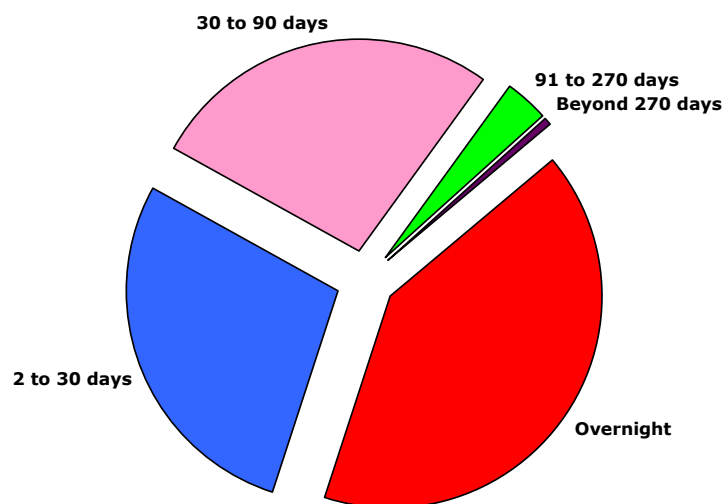


Maturity Characteristics

The maturity of the private extensions of unsecured credit (i.e., exclusive of that to GSEs and other FHLBanks) is quite short. The Financial Management Policy (FMP), which governs the investments of those FHLBanks that have not implemented their capital plan, generally limits unsecured extensions of credit, except for the net unsecured credit arising from derivatives contracts, to no more than 270 days.

Forty-one percent of the private extensions of credit at January 31, 2003, had an overnight maturity and an additional 28 percent had a remaining maturity of less than 30 days.

**Maturity Distribution of Private Unsecured Credit
Of the FHLBanks at January 31, 2003**

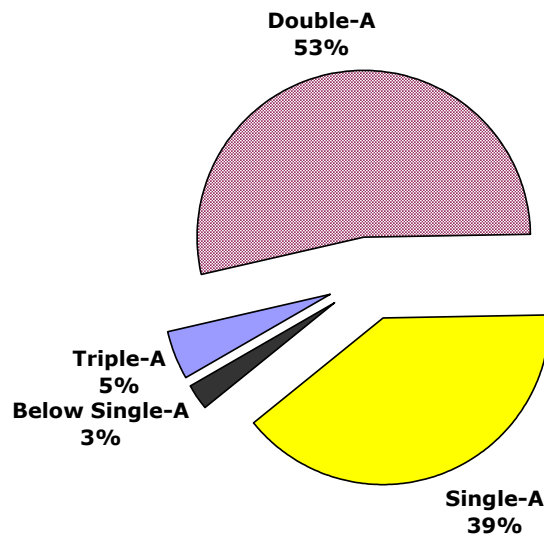


Credit Characteristics of the Private Unsecured Credit

The preponderance of the private unsecured credit extensions of the FHLBanks is with issuers whose long-term rating is either double-A (53%) or single-A (39%). There are few eligible domestic or foreign counterparties with triple-A long-term ratings.

Approximately half of the private unsecured credit extensions of the FHLBanks are to the domestic branch and agency offices of foreign banking organizations.

**Average Credit Quality of Private Unsecured Credit
March 2002 through January 2003**

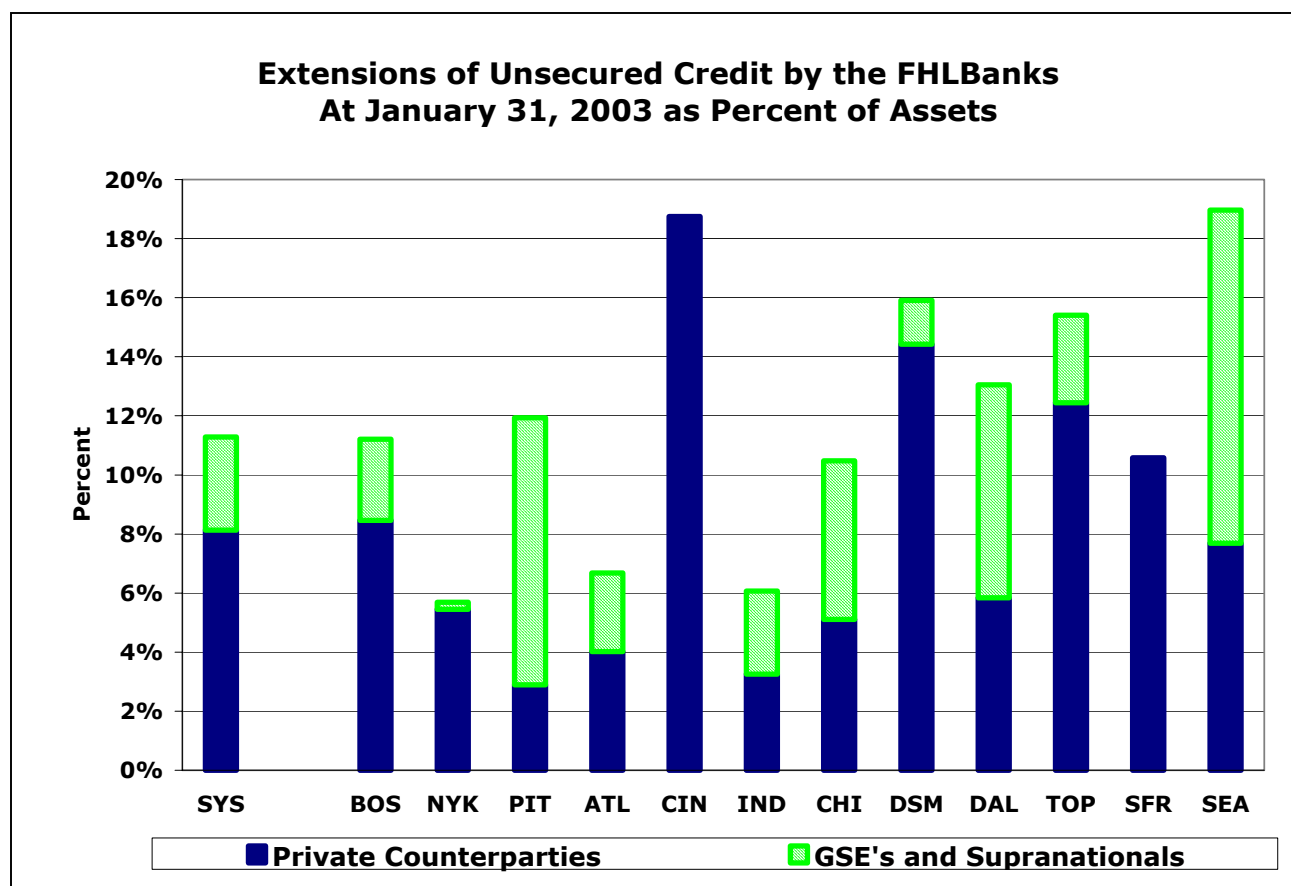


FHLBank Unsecured Investments

As of January 31, 2003, unsecured investments of the FHLBanks aggregated to 11.4 percent of total assets. Included in this total are investments in the debt obligations of other GSEs that aggregate to 3.2 percent of the FHLBanks' assets. Both total unsecured investments and investments in the debt of other GSEs vary considerably across the FHLBanks.

At January 31, 2003, 6 of the 12 FHLBanks had extensions to their largest counterparty in excess of 25 percent of the FHLBank's capital.

Total System extensions to the 10 largest counterparties were 39 percent of the total private unsecured credit extensions. Five of these 10 counterparties are domestic branch and agency offices of foreign banking organizations and 4 are domestic bank holding companies. Total System extensions to the largest counterparty were \$4.3 billion.



Current Unsecured Credit Limitations -- 12 CFR § 932.9

A. Limits to Individual Private Counterparties for Other Than Overnight Transactions

Long-term Rating	Short-term Rating If Counterparty Does Not Have Long-Term Rating	Percentage Applied to the Lesser of the FHLBank's or Counterparty's Capital
Highest Investment Grade		15
Second Highest Investment Grade		14
Third Highest Investment Grade	Highest Short-term Rating	9
Fourth Highest Investment Grade	2nd and 3rd Highest Short-term Rating	3
Below Investment Grade		1

B. Limits on Overnight Credit

Total overnight and term credit to a single counterparty may not exceed twice the limits in the table.

C. Affiliated Counterparties

Total unsecured credit to affiliated counterparties may not exceed 30 percent of the FHLBank's capital.

D. GSE Limits

Total unsecured credit to any GSE shall not exceed the lesser of the FHLBank's or the GSE's capital.

E. Credit to an FHLBank

Unsecured extensions of credit from one FHLBank to another FHLBank are exempt from the unsecured credit limits.

Determination of Applicable Ratings

- ❑ Most recent rating
- ❑ Use the lower rating if more than one Nationally Recognized Statistical Rating Organization (NRSRO) has rated the issuer or obligation.
- ❑ If the credit rating has a modifier, the modifier is not used.
- ❑ If the counterparty is on a watch list for a downgrade, the applicable rating is the next lower rating from that NRSRO. In the case of a downgrade, the FHLBank need not unwind the position. However, the FHLBank may make additional credit extensions, including the renewal of existing extensions of credit, only at the new lower limit.
- ❑ If a counterparty is not rated, then the FHLBank should use credit rating standards available from an NRSRO or similar standards.

Reporting Requirements

- ❑ Each FHLBank must report monthly to the Finance Board on total extensions of unsecured credit to any counterparty or affiliated group of counterparties that exceed the greater of 5 percent of the FHLBank's or counterparty's capital. This reporting is done through the monthly unsecured credit report prepared by the Office of Finance.
- ❑ Each FHLBank must report monthly to the Finance Board on total secured and unsecured extensions of credit that exceed 5 percent of the FHLBank's assets. The limitation applies to either a single counterparty or an affiliated group of counterparties. This reporting is done through the call report.
- ❑ Each FHLBank must promptly report to the Finance Board on any extensions of credit that are in excess of the regulatory limits. This reporting is done through exception reporting to the Office of Supervision.

Carry-over Provisions from the Financial Management Policy

- ❑ Until an FHLBank implements its capital plan, it is subject to several provisions of the Financial Management Policy (FMP) dealing with unsecured credit.
- ❑ The remaining maturity may not exceed nine months for fed funds, resale agreements, U.S. dollar deposits, commercial paper, and bankers' acceptances. While the maturity limitation ceases to be effective when a capital plan is implemented, the FHLBank must file a new business activity notice if it wishes to purchase unsecured obligations of private counterparties that exceed the nine-month maturity.
- ❑ Eligible financial institutions include FHLBanks or FDIC-insured financial institutions, including subsidiaries of foreign commercial banks, that have Tier I capital of at least \$100 million if a member and \$250 million if a non-member.
- ❑ Eligible counterparties for resale agreements include the Federal Reserve Bank of New York, primary dealers recognized by the Federal Reserve Bank of New York, whose capital exceeds \$250 million or whose obligations are guaranteed by parent firms that have at least \$250 million of capital, and government-sponsored enterprises.
- ❑ Eligible issuers for commercial paper must be in the banking, housing, finance, or securities industries. The issuer must have tangible capital of at least \$100 million if a member and \$250 million if a non-member.

Comparison to Former Limits Contained in the FMP

The investment limits formerly contained in the FMP were considerably more liberal than new limits contained in the unsecured credit rule, principally because issuers with the highest short-term credit ratings received the most favorable treatment irrespective of their long-term rating. Very few issuers have the highest long-term rating, but many more issuers have the highest short-term rating.

Rating	FMP Limit – Percent of FHLBank Capital	Limit in Unsecured Credit Rule on Term Extensions of Credit	Limit in Unsecured Credit Rule on Total Extensions of Credit
Highest Short-term	30	9 if no long-term rating	18 if no long-term rating
Highest Long-term	30	15	30
Second Highest Long-term	20	14	28
Third Highest Long-term	10	9	18

The FMP also contained a 25 percent limitation on extensions of unsecured credit based on the counterparty's Tier I capital.

Note: The preferred ratings in the FMP for bank issuers were Thomson Bank Watch ratings, which were primarily short-term ratings. Thomson Bank Watch ratings are no longer available.

Comparison to Limits Contained in the December 2000 Capital Rule

The final capital rules adopted in December 2000 contained new limits on total (term and overnight) extensions of unsecured credit to any single counterparty.

	December 2000 Capital Rule	Current Regulatory Limit Term Credit	Current Regulatory Limit Total Credit
Highest Investment Grade	15	15	30
Second Highest Investment Grade	12	14	28
Third Highest Investment Grade	6	9	18
Fourth Highest Investment Grade	1.5	3	6
Below Investment Grade	1	1	2

In the December 2000 rule, overnight credit received no special treatment, and combined extensions to all affiliated counterparties had to fit within the limits. The limits in the December 2000 rule were amended and liberalized before they became effective.